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FEMA's Community Disaster Loan (CDL) Program: A Primer

Following a major disaster, local governments may face fiscal and economic distress as well as physical damage. As a result, revenue shortfalls could impact both service delivery and the long-term fiscal health in the affected locality. To address these issues, the Federal Emergency Management Agency (FEMA) offers the Community Disaster Loan (CDL) program, which provides forgivable loans capped at $5 million to units of local government based on real revenue shortfalls.

This In Focus examines the basic structure of the CDL program and also briefly considers two CDL variants developed in response to distinct disaster situations.

Overview of the CDL Program

CDL Program Purpose and Characteristics

CDLs were first authorized in the Disaster Relief Act of 1974 (P.L. 93-288) but were defined and established by the Stafford Act (P.L. 100-707), which amended and renamed the preceding Disaster Relief Act. CDLs were developed to help local governments (as defined by the Stafford Act) manage acute tax and other revenue loss after a major disaster, which could inhibit their ability to adequately serve their communities during recovery. CDLs are funded through the Direct Assistance Disaster Loan Program (DADLP), to which Congress may appropriate funds directly for CDL program purposes. More commonly, however, funds are transferred to the DADLP from the Disaster Relief Fund—the fund which supports most federal disaster relief operations.

The CDL program offers forgivable loans to units of local government equal to the amount of the revenue shortfall caused by the disaster up to 25% of the locality's operating budget, with a maximum of $5 million. Under the conventional program, those funds may be utilized to provide any normal governmental service or for services necessary to respond to the disaster. CDLs are five-year loans, extendable to 10 years at FEMA's discretion, with interest rates determined by the Treasury Secretary.

CDL Qualifying and Applying

To qualify for a conventional CDL, an applicant local government must:

- Be located in a presidentially declared disaster area;
- Show substantial loss (greater than 5%) of tax and other (such as administrative) revenues;
- Not be in arrears on any other previous CDL loans; and
- Be permitted to take federal loans under its respective state law.

A local government meeting these criteria may be eligible to apply for a CDL, and may apply from the end of the disaster, as determined by FEMA, through the end of the following fiscal year. FEMA calculates loan amounts by estimating cumulative revenue loss for the fiscal year of the disaster and the subsequent three fiscal years, up to 25% of the local government's total budget for the fiscal year when the disaster occurred (or the subsequent fiscal year).

If the estimated revenue loss equals 75% of the locality's budget for the fiscal year of the disaster, the CDL may exceed the 25% threshold up to 50% of the operating budget. Loans may not exceed a $5 million statutory cap.

To initiate the application process, FEMA assists local governments with eligibility screening, loan qualification estimates, and application development in advance of a formal application. Localities then formally apply for the CDL through their state (or territory) Governor's Authorized Representative, who requests activation of the CDL Program from FEMA. Federally recognized tribal governments may also be eligible for CDLs directly following a major tribal disaster declaration.

CDL Forgiveness

FEMA may forgive all or part of the CDL if a local government can demonstrate that it has a three-year operating deficit following and associated with the disaster. This may include increases in operating expenditures as a result of unreimbursed disaster-related expenses.

To adjudicate forgiveness eligibility, FEMA reviews audited financial statements of the local government borrower for the three years following the disaster. The review has two parts: (1) a deficit analysis; and (2) a revenue analysis. The deficit analysis compares revenues and expenditures for the full three calendar years following the disaster. If the analysis shows a deficit, FEMA conducts the revenue analysis, which compares pre-disaster revenues against operating revenues to determine the existence of a three-year cumulative revenue loss.

If the analysis shows a deficit and a loss, the lesser of the two is used to provide either partial or full forgiveness. If a surplus is found, the local government is ineligible for cancelation, and the loan must be repaid according to the terms of the promissory note issued with the disbursement.

Recent CDL Program Variants

In extraordinary circumstances, Congress has authorized FEMA to administer non-traditional CDLs and CDL-type programs with different eligibility and technical requirements. Unlike traditional CDLs, these loans are not subject to the $5 million cap, and eligible areas are more geographically concentrated. While these programs have at times operated in parallel to the conventional CDL program, they were temporary programs and not separately authorized.

The "Special" CDL Program

As part of the federal response to extensive economic damage caused by Hurricanes Katrina and Rita, Congress passed legislation in 2005 (P.L. 109-88) and 2006 (P.L. 109-234) to make approximately $1 billion available to support nearly $1.4 billion of special CDLs. These temporary CDLs were made available in October 2005, or approximately two months following the Hurricane Katrina disaster that August.

The special CDL program was focused on areas affected by Hurricanes Katrina and Rita in the Gulf Coast region, and provided funds beyond the $5 million cap, albeit still at the 25% budget limit. Funds were limited to "essential services," as opposed to any eligible municipal service under conventional CDLs, and localities were eligible for more than one CDL. While the temporary special CDLs initially prohibited forgiveness, 2007 legislation (P.L. 110-28) mandated that forgiveness be allowed. Additional legislation expanded forgiveness criteria that effectively forgave the majority of outstanding CDLs (P.L. 113-6).

CDL-Type Instrument for Puerto Rico and USVI

Following Hurricanes Harvey, Irma, and Maria, Congress passed legislation (P.L. 115-72) providing funding for temporary CDL-type loan instruments for Puerto Rico and the U.S. Virgin Islands (USVI). Although based on the conventional CDL program, the resulting program was functionally different due to significant exceptions and modifications, including the following:

- Territorial governments were considered municipalities for the purposes of the program;
- The $5 million cap was lifted;
- Loan recipients (i.e., territorial governments) were allowed to receive more than one loan;
- Loans could only be forgiven at the discretion of the Secretary of Homeland Security in consultation with the Secretary of the Treasury; and
- The Secretary of Homeland Security, in consultation with the Secretary of the Treasury, solely determined the "terms, conditions, eligible uses, and timing and amount" of such loans.

The CDL-type instrument's statutory provisions related to loan forgiveness and terms were further complicated by Puerto Rico's broader fiscal crisis and the existence of a federal oversight board, as established by the Puerto Rico Oversight, Management, and Economic Stability Act of 2016 (PROMESA; P.L. 114-187). Without greater surety over forgiveness, and already constrained by PROMESA, the Puerto Rican government chose not to avail itself of the CDL-type instrument.

Policy Issues for Congress

Should the rate and severity of disaster-related damages continue or accelerate, traditional CDLs or their non-traditional analogues may be increasingly utilized. However, due to their relatively low funding cap and specialized nature, conventional CDLs may be inadequate for widespread and severe disaster events. During the COVID-19 pandemic, for example, uptake of the CDL program does not appear to be widespread, perhaps due to the severity of the crisis, and because it is still ongoing (compared to more time-bound disasters in the past)—though a governor may still be able to initiate a request.

Instead, states and localities have turned to alternative mechanisms to address the fiscal challenges posed by the pandemic. In the current economic environment, conventional CDLs may be an insufficient countermeasure due to the scale of potential revenue loss, and the indeterminate nature of the crisis. No special CDLs have been authorized by Congress in response to the pandemic. However, Congress may consider a special pandemic CDL that allows for higher budget thresholds (beyond the $5 million cap), disbursement prior to the end of the pandemic, and well-defined forgiveness criteria.

Congress may also consider structuring traditional CDLs more expansively to account for a wider universe of disaster and emergency scenarios, such as state- or executive agency-based disaster declarations, expanding or lifting the $5 million cap, or simplifying the forgiveness process. In addition, the CDL program's loan forgiveness facility could be expanded to account for situations where the recipient would be especially harmed if it were made to repay all or part of the CDL loan. Another option could be to change it from a forgivable loan to a grant program.

Another potential alternative would be to restructure CDLs with automatic forgiveness thresholds based on predetermined triggering criteria. For example, tranches of the CDL loan could be automatically forgiven based on alternative factors such as the severity of the disaster, the fiscal position of the local government, and/or the potential impact that repayment may have on the locality's future provision of governmental services. This could "automate" the program and provide greater surety to localities regarding issues of forgiveness and repayment.

More broadly, Congress could also develop other disaster assistance instruments that separately address immediate governmental liquidity, disaster response, and long-term recovery needs. Following a disaster, one locality may require immediate financial liquidity but may be otherwise positioned to weather the crisis in the longer-term, while another locality may need more extensive assistance with long term recovery.

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